



July 14, 2015

MEMORANDUM

To: Lisa J. Stevenson
Deputy General Counsel - Law

AUDIT REFERRAL 15-06

Through: Alec Palmer
Staff Director

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Chief Compliance Officer

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Subject: Gary Johnson 2012, Inc - Referral Matters

On June 29, 2015, the Commission approved the Proposed Final Audit Report on Gary Johnson 2012, Inc. The report was released to the public on July 8, 2015. In accordance with the Materiality Thresholds for Title 26 Primary Election Committees, the Final Audit Report of the Commission includes findings that meet the criteria for referral to the Office of General Counsel.

Finding 3 – Use of General Election Contributions for Primary Election
Expenses: Amount in Violation \$12,396; Calendar Year 2012
Finding 4 – Reporting of Debts and Obligations: Amount in Violation \$447,567;
Calendar Years 2011 and 2012

Currently, this committee is involved in an on-going OGC matter (MUR #6639).

All workpapers and related documentation are available for review in the Audit Division. Should you have any questions regarding this/these matter(s), please contact Lead Auditor or Audit Manager at 694-1200.

Attachments: Finding 3 – Use of General Election Contributions for Primary Election Expenses
Finding 4 – Reporting of Debts and Obligations
Designation of Counsel

Finding 3. Use of General Election Contributions for Primary Election Expenses

Summary

During audit fieldwork, the Audit staff's review of GJ2012's receipts and disbursements during the pre-DOI period indicated that GJ2012 spent \$12,396 in general election receipts on primary election expenses prior to the Candidate's DOI.

In response to the Preliminary Audit Report, GJ2012 stated that the use of general election receipts for primary election expenses was an advance against anticipated matching funds. The Audit staff noted that short-term advances against matching funds must come from a qualified financial institution, and be secured by certified matching funds amounts. The Commission approved a finding that GJ2012 used \$12,936 in general election contributions for primary election expenses prior to the general election.

Legal Standard

Receipt of General Election contributions before the date of the Primary Election.

(1) If the candidate, or his or her authorized committee(s), receives contributions that are designated for use in connection with the general election pursuant to 11 CFR §110.1(b) prior to the date of the primary election, such candidate or such committee(s) shall use an acceptable accounting method to distinguish between contributions received for the primary election and contributions received for the general election. Acceptable accounting methods include, but are not limited to:

- (i) The designation of separate accounts for each election, caucus or convention; or
- (ii) The establishment of separate books and records for each election.

(2) Regardless of the method used under paragraph (e)(1) of this section, an authorized committee's records must demonstrate that, prior to the primary election, recorded cash-on-hand was at all times equal to or in excess of the sum of general election contributions received less the sum of general election disbursements made. 11 CFR §102.9(e).

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff reviewed available receipt and disbursement records to determine what contributions, if any, were designated per contributor solicitation devices to the general election and then spent by GJ2012 on primary election expenses prior to the primary election date (May 5, 2012). Committees are not permitted to spend funds designated to the general election for primary election expenses prior to the primary election date. If general election funds are held in the primary election account, the general election funds should be held in reserve and not spent for primary election purposes.

Prior to the primary election, GJ2012 received a total of \$22,396 designated to the general election that was deposited in the primary election account. The Audit staff determined the private contributions designated for the general election using the same calculations as were employed in the Statement of Reasons In Support of Final Determination of Entitlement in the

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Matter of Governor Gary Johnson (LRA #905), dated November 14, 2013. Of this amount, a total of \$10,000 was deposited to the general election account by September 6, 2011. Beginning on February 21, 2012, GJ2012 did not maintain enough contributions designated to the primary election to pay for all of its primary expenditures, and used contributions designated to the general election to make up the difference. The Audit staff's review identified \$12,396 in contributions designated to the general election that were spent on primary election expenses prior to the primary election date. These expenditures were identified as primary election expenses as they were bank fees incurred prior to the Candidate's DOI and payments on invoices submitted for various services incurred in connection with the Candidate's campaign for nomination. In addition, no invoices for any services rendered in conjunction with the general election were received prior to the payment of these expenses.

B. Preliminary Audit Report & Audit Division Recommendation

The Audit staff presented this matter to GJ2012 representatives at the exit conference and provided schedules detailing the payments made using general election funds for primary election expenses prior to the candidate's DOI for the audited cycle. GJ2012 representatives did not comment on this finding.

The Audit staff recommended that GJ2012 provide documentation to demonstrate that general election contributions were not used to fund primary election activity. In accordance with 11 CFR §102.9, documentation should demonstrate that an acceptable accounting method was used. Absent such a demonstration, GJ2012 was to provide any additional comments it considered necessary with respect to this matter.

C. Committee Response to Preliminary Audit Report

In response to the Preliminary Audit Report recommendation, GJ2012 stated that the \$12,396 was treated as an advance against anticipated matching funds from the general election contributions to the primary election.

To the extent that GJ2012 is characterizing the advance of general election funds as a loan to the primary account, it is noted that regulations specify that such loans or advances must come from a qualified financial institution, which the general account is not. It is also noted that short term loans to Presidential primary committees were obtained in the past, however, these loans were secured by matching fund amounts certified and expected to be received by the committees and occurred only when the Presidential Campaign fund was in a shortfall position. Matching funds for GJ2012 were not certified until May 25, 2012 and the Presidential Campaign fund was not in a shortfall position in 2012. In no instances were general election contributions permitted to be used for primary election expenditures.

GJ2012 stated that they "...used an acceptable accounting method in accordance with 11 CFR §102.9," and that there were separate accounts for primary and general election contributions. As explained in the "Committee Structure" section on pages 1 and 2 of this report, in practice, GJ2012 deposited nearly all receipts before DOI in its designated primary account and nearly all receipts after DOI in its designated general account. GJ2012 further stated that Audit staff based its calculation on cash on hand and did not take into account the delay in deposits collected through credit card processors. These would be considered received, but would not be in GJ2012's bank account immediately.

In fact, as this is a common occurrence with campaign committees, the Audit staff took this deposit delay into account. The Audit staff used GJ2012's contributions database for this calculation, which uses the date of contribution rather than the date of deposit.

D. Draft Final Audit Report

The Draft Final Audit Report acknowledged GJ2012's statement that the use of general election contributions was treated as an advance against anticipated matching funds, but the Audit staff disputed that an advance from general election contributions rather than from a lending institution was allowable.

E. Committee Response to the Draft Final Audit Report

In response to the Draft Final Audit Report, GJ2012 requested that the arguments made in response to the Preliminary Audit Report be reconsidered and requested an audit hearing to present its arguments.

F. Audit Hearing

During the audit hearing, Counsel agreed that GJ2012 did use general election contributions for primary election expenses. However, Counsel stated that these were only to cover short term gaps in cash flow and it would have been a burden to seek outside funds for such short term matters. Counsel stated that the finding lacks context, and that it seems unreasonable and not the intent of the Act to force committees to engage in commercial transactions in order to cover such short term cash flow issues. Counsel emphasized that these were short-term loans only, and stated that he thought that it would be easy to tell if any committee was abusing this leeway.

Commission Conclusion

On June 18, 2015, the Commission considered the Audit Division Recommendation Memorandum in which the Audit staff recommended the Commission find that GJ2012 used \$12,936 in general election contributions for primary election expenses prior to the general election.

The Commission approved the Audit staff's recommendation.

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Finding 4. Reporting of Debts and Obligations

Summary

During audit fieldwork, the Audit staff's review of GJ2012's disbursements indicated that debts from seven vendors totaling \$407,455 were not disclosed on Schedule D-P (Debts and Obligations), as required.

In response to the Preliminary Audit Report, GJ2012 submitted additional invoices for debts to two vendors that were not previously disclosed to Audit staff. This resulted in a total of \$447,567 in debts owed to nine vendors that were not disclosed on Schedule D-P as required. GJ2012 amended its reports to materially correct the disclosure of debts and obligations on Schedule D-P.

The Commission approved a finding that that GJ2012 did not disclose debts to nine vendors totaling \$447,567, as required.

Legal Standard

A. Continuous Reporting Required. A political committee must disclose the amount and nature of outstanding debts and obligations until those debts are extinguished.

52 U.S.C. §30104(b)(8) and 11 CFR §§104.3(d) and 104.11(a).

B. Separate Schedules. A political committee must file separate schedules for debts owed by and to the committee with a statement explaining the circumstances and conditions under which each debt and obligation was incurred or extinguished. 11 CFR §104.11(a).

C. Itemizing Debts and Obligations.

- Once it has been outstanding 60 days from the date incurred, a debt of \$500 or less must be reported on the next regularly scheduled report.
- A debt exceeding \$500 must be disclosed in the report that covers the date on which the debt was incurred, except reoccurring administrative expenses (such as rent) shall not be reported as a debt before the payment due date. 11 CFR §104.11(b).

Facts and Analysis

A. Facts

During audit fieldwork, the Audit staff used available disbursement records to reconcile the accounts¹ of GJ2012's vendors.² These vendors provided GJ2012 with various campaign management services such as fundraising, accounting, clerical and administrative staff, and travel arrangements.

¹ The reconciliation consisted of calculating invoiced and paid amounts for individual reporting periods in the 2011-2012 campaign cycle. The Audit staff then determined whether any outstanding debts were correctly disclosed on Schedule D-P. Each debt amount was counted once, even if it required disclosure over multiple reporting periods.

² The Audit staff restricted this review to only primary campaign debts, as per the scope of this Audit.

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The Audit staff identified debts to seven of GJ2012's vendors totaling \$407,455 that were not reported on Schedule D-P as required. Of these debts, \$300,000 was owed to NSON for a bonus after the Candidate received the nomination as the Libertarian Party candidate for the Presidential general election. This bonus was incurred, per contract, as of the date of nomination, May 4, 2012, and should have been reported on the 2012 June Monthly report, covering the time period from May 1, 2012 through May 31, 2012.

It should be noted that GJ2012 was invoiced for half of this debt (\$150,000) on December 21, 2012, and reported it on the 2012 Year-End report. However, the Audit staff maintains the debts should have been reported as debt for the entire amount based on the date and terms of the contract. The remaining reportable debts of \$107,455 were for smaller amounts to all six vendors identified by the Audit staff.

B. Preliminary Audit Report & Audit Division Recommendation

The Audit staff presented this matter to GJ2012 representatives at the exit conference and provided schedules detailing the unreported debts for each reporting period covered by the audit. In response to the exit conference, GJ2012 submitted one additional invoice for the other half of the bonus referenced in the "Facts" section above. This invoice was dated January 1, 2013. As of the date the Preliminary Audit Report was sent to GJ2012, this \$150,000 had not been disclosed on any reports filed with the Commission.

The Audit staff recommended that GJ2012 provide documentation demonstrating that these expenditures did not require reporting on Schedule D-P. Absent such documentation, the Audit staff recommended that GJ2012 amend its reports to disclose the outstanding debts.

C. Committee Response to Preliminary Audit Report

In response to the Preliminary Audit Report recommendation, GJ2012 amended its reports and submitted additional invoices and documentation for other previously undisclosed debts. Adjustments made by the Audit staff based on the additional documentation provided reduced the original determination of debts and obligations not timely reported amount by \$7,758.

GJ2012 submitted additional invoices from two new vendors that were not previously provided to the Audit staff, nor disclosed on Schedule D-P, for debts incurred within the audit period totaling \$47,870. In combination with the seven vendors noted in the Preliminary Audit Report, the Audit staff has thus identified nine vendors that GJ2012 owed \$447,567 that was not reported on Schedule D-P as required. GJ2012 filed amendments that materially corrected these omissions.

In its initial response to the Preliminary Audit Report, GJ2012 disputed that the \$300,000 owed to NSON for a bonus was not timely reported. GJ2012 states that the NSON contract "...specifically states that invoices are due and payable upon receipt," and that the vendor not invoicing timely does not create a reportable debt, since the campaign would not be able to base the debt reporting on an invoice.

Pursuant to 11 CFR §104.11(b), "[a] debt or obligation, including a loan, written contract, written promise or written agreement to make an expenditure...shall be reported as of the date on

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which the debt or obligation is incurred..." GJ2012 made a written agreement on October 14, 2011, that NSON would be owed a bonus of "\$300,000 for receiving any party nomination as either VP or President." Thus, this debt was incurred on the date of the Candidate's nomination by the Libertarian Party at its convention on May 5, 2012, and should have been reported as a debt or obligation on Schedule D-P on the June Monthly Report that covered May 1, 2012 through May 31, 2012, regardless of when it was invoiced.

In a supplemental response to the Preliminary Audit Report, GJ2012 stated that it has deferred to Audit staff's judgment that the \$300,000 win bonus should be reported as of the date of the Candidate's nomination, despite not having been invoiced.³ GJ2012 filed amendments to its reports to report this obligation as of May 2012.

D. Draft Final Audit Report

The Draft Final Audit Report acknowledged that GJ2012 filed amendments to materially correct its reporting of debts and obligations.

E. Committee Response to the Draft Final Audit Report

In response to the Draft Final Audit Report, GJ2012 discussed its method of accounting, in which GJ2012 "re-allocated payments" in December of 2014 to pay off \$171,000 of the \$300,000 win bonus within the 30-day regulatory requirement, so that the \$171,000 would be considered a qualified expense.⁴ GJ2012 also requested an audit hearing to address this matter.

F. Audit Hearing

During the audit hearing, Counsel stated that GJ2012 had amended its reports to correctly report debts and obligations, and that there were no further substantive comments regarding this finding.

Commission Conclusion

On June 18, 2015, the Commission considered the Audit Division Recommendation Memorandum in which the Audit staff recommended the Commission find that GJ2012 did not disclose debts to nine vendors totaling \$447,567, as required.

The Commission approved the Audit staff's recommendation.

³ GJ2012 further stated that they, "in conjunction with NSON, reallocated prior payments to NSON to this earlier Primary expenditure to ensure that payments were made on a First in-First out basis." The Audit staff believes that GJ2012 cannot reallocate these payments in such a manner. It appears that GJ2012 has decided to apply this procedure in an attempt to reduce the amount of repayment to the U.S. Treasury as detailed in Finding 2. However, this "re-allocation" of payments would still not result in the win bonus being paid within the statutory 30 day period (see footnote 20 for additional detail), so this remains a non-qualified expense regardless of the accounting convention used. In fact, to alter the accounting method to pay this debt off would result in additional non-qualified expenses paid using matching funds, which would actually result in an even larger repayment to the U.S. Treasury.

⁴ This argument pertains to the calculations in Finding 2 of non-qualified expenses, not to the substance of Finding 4.



FEDERAL ELECTION COMMISSION

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STATEMENT OF DESIGNATION OF COUNSEL

Please use one form for each Respondent/Entity/Treasurer

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MUR # Preliminary Audit Report of Gary Johnson 2012 Inc.

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The above-named individual and/or firm is hereby designated as my counsel and is authorized to receive any notifications and other communications from the Commission and to act on my behalf before the Commission.

12/18/14
Date

Chet Goodwin
Respondent/Agent-Signature

TREASURER
Title (Treasurer/Candidate/Owner)

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Information is being sought as part of an investigation being conducted by the Federal Election Commission and the confidentiality provisions of 2 U.S.C. § 437g(a)(12)(A) apply. This section prohibits making public any investigation conducted by the Federal Election Commission without the express written consent of the person under investigation